

Hexcel Corporation (HXL)

\$40.12 (As of 08/05/20)

Price Target (6-12 Months): **\$43.00**

Long Term: 6-12 Months

Zacks Recommendation:
Neutral

(Since: 06/29/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

4-Sell

Zacks Style Scores:

VGM:C

Value: B

Growth: C

Momentum: F

Summary

Hexcel Corp. ended second quarter of 2020 on a mixed note. While its earnings missed the Zacks Consensus Estimate, revenues beat the mark. To compete in the diverse industries in which the company caters to, Hexcel Corp. consistently innovates next-generation products and collaborate with companies. Although the company's long-term debt remains much higher than its cash reserve, its current debt is much lower than the cash balance. This reflects its solid solvency level at least in the near term. However, rapid spread of coronavirus across the globe caused a notable decline in air travel, thereby hurting Hexcel. The outbreak forced the company to terminate its pending merger deal with Woodward and temporarily suspend its dividend payout and share buyback programs. Hexcel's shares have underperformed its industry in the past year.

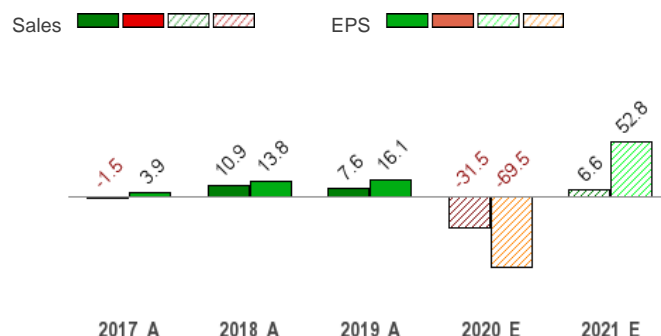
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$87.00 - \$24.54
20 Day Average Volume (sh)	863,610
Market Cap	\$3.4 B
YTD Price Change	-45.3%
Beta	1.15
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Aerospace - Defense Equipment
Zacks Industry Rank	Bottom 14% (218 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-60.0%
Last Sales Surprise	10.2%
EPS F1 Est- 4 week change	-14.5%
Expected Report Date	10/19/2020
Earnings ESP	0.0%
P/E TTM	16.2
P/E F1	37.2
PEG F1	3.7
P/S TTM	1.6

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	439 E	447 E	456 E	466 E	1,721 E
2020	541 A	379 A	345 E	361 E	1,615 E
2019	610 A	609 A	573 A	564 A	2,356 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.38 E	\$0.42 E	\$0.47 E	\$0.51 E	\$1.65 E
2020	\$0.64 A	\$0.08 A	\$0.13 E	\$0.24 E	\$1.08 E
2019	\$0.84 A	\$0.94 A	\$0.90 A	\$0.86 A	\$3.54 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/05/2020. The reports text is as of 08/06/2020.

Overview

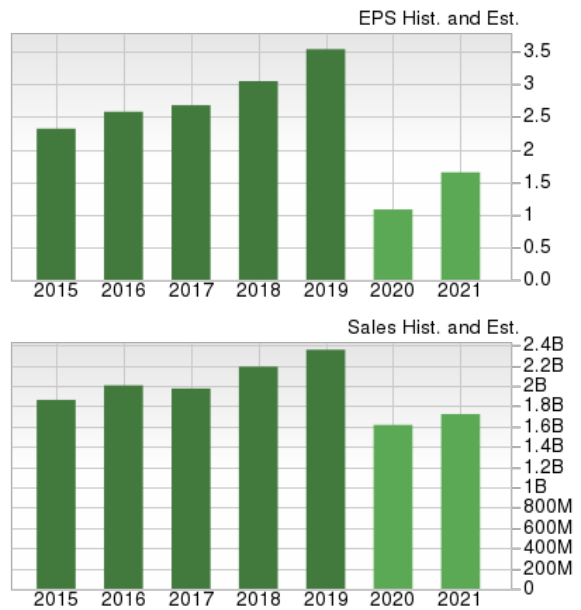
Delaware-based Hexcel Corporation develops, manufactures and distributes lightweight, high-performance structural materials for use in the Commercial Aerospace, Space & Defense and Industrial markets. Hexcel Corporation, founded in 1946, was incorporated in California in 1948, and reincorporated in Delaware in 1983. The company's products are used in a wide variety of end applications, such as commercial and military aircraft, space launch vehicles and satellites, wind turbine blades, automotive and other complex industrial applications. The company serves international markets through manufacturing facilities located in the United States, Asia Pacific, Europe, Russia and Africa.

Hexcel Corporation operates in two business segments namely the Composite Materials and Engineered Products.

The **Composite Materials** segment manufactures and markets carbon fibers, fabrics and specialty reinforcements, prepregs and other fiber-reinforced matrix materials, structural adhesives, honeycomb, molding compounds, tooling materials, polyurethane systems and laminates that are incorporated into military and commercial aircrafts, wind turbine blades, recreational products, automobiles and other industrial applications. Net sales for this segment were \$1,946.5 million in 2019, representing 82.6% of the company's total sales.

The **Engineered Products** segment manufactures and markets composite structures and precision machined honeycomb parts primarily for use in the aerospace industry. Composite structures are manufactured from a variety of composite and other materials, including prepregs, honeycomb, and structural adhesives, using manufacturing processes like autoclave processing, multi-axis numerically controlled machining, heat forming, and other composite manufacturing techniques. Net sales for this segment were \$493.4 million in 2019, representing 20.9% of the company's total sales.

However, total sales included corporate expenses of \$84.2 million.



Reasons To Buy:

- ▲ During the second quarter of 2019, Hexcel Corp announced its financial outlook through 2021 long with its other long-term targets. For the three-year period 2019 to 2021, the company expects total sales to witness a compounded annual growth rate (CAGR) of 6-9%. Strong commercial aerospace programs, continued growth in the F35 Joint Strike Fighter build rate and consistent growth in other fixed wing programs are expected to drive Hexcel Corp.'s growth. Also, double-digit demand growth for its wind energy products are expected to contribute to the top line.

Hexcel Corp further anticipates adjusted diluted earnings per share to grow at a double-digit rate, supported by operational excellence and a total capital expenditure of \$500-\$550 million during the three-year period. The company also expects continued expansion of free cash flow generation, providing a total of \$1.8 billion between 2019 and 2023, which will be available for continued investment in organic growth, strategic acquisitions and to return to its shareholders.

- ▲ To compete in the diverse industries in which the company operates, Hexcel Corp. consistently brings in next-generation products to the market and also enters into collaborations to capture market share. In April 2020, the company launched a low temperature fast cure HexBond 679 adhesive film. Notably, HexBond 679 adhesive films allow boatbuilders to increase build rates with reduced heating and cooling times. Earlier, in February 2020, Hexcel Corp. collaborated with NaCa Systems, a Tier 1 supplier of natural fiber composite automotive interior parts, on the development of a lightweight carbon fiber prepreg and wood fiber composite sports car seat back using a rapid press molding process. This innovation validates a short-cycle time production process for CFRP and wood fiber composite parts and offers a host of benefits to automotive manufacturers. Such innovations and collaborations should bolster this stock's growth over the long run.
- ▲ Hexcel ended the second quarter of 2020 with cash and cash equivalents of \$257 million compared with \$329 million as of Mar 31, 2020. The company's long-term debt of \$1,265 million as of Jun 30, 2020 was lower than \$1,390 million as of Mar 31, 2020. Although the company's long-term debt remains much higher than the cash reserve, its current debt worth \$1 million is much lower than the cash balance. So, this is good news for the company's solvency level at least in the near term.

Moreover, the company's current ratio of 3.86 as of Jun 30, 2020 rose from 3.36 as of Mar 31, 2020. This is encouraging, considering the fact that a current ratio of more than 1 indicates the company's capability to pay off its short-term obligations. Moreover, to cope with the impact of the virus outbreak, Hexcel has started implementing significant reductions in its U.S. workforce, as well as short-term cost savings actions, including temporary salary reductions, unpaid furloughs, and suspension of employee stock purchase plan. We expect such initiatives to shield the company from a loss, at least in the near term.

Steady innovations and solid investment plans are expected to boost Hexcel Corp.

Reasons To Sell:

- ▼ Lower deliveries for Boeing's 737 jets continued during the second quarter of 2020, following the grounding of these jets in March 2019. Notably, Boeing announced a temporary production rate decrease to 42 planes per month in April 2019 from 52 produced before. In December, Boeing announced its decision to temporarily suspend the production of its once fastest-selling jet. Such consecutive setbacks in the 737 Max program affected part suppliers like Hexcel.

The company's Engineered Product segment, which comprises Hexcel's structures and engineered core businesses, incurred an operating loss of \$0.5 million against operating income of \$16.3 million in the year-ago quarter. This can be primarily attributed to the 737 MAX crisis. Moreover, the company's commercial aerospace sales suffered an annual revenue loss of 52% in the reported quarter, with lower sales from 737 Max being a major contributor.

- ▼ Owing to the rapid spread of coronavirus across the globe, dramatic decline in air travel along with stringent restrictions on businesses has led to significant declines in demand both within the aerospace and industrial markets. Consequently, Hexcel has announced dismal quarterly figures so far in 2020, with the continued grounding of the Boeing 737 MAX and effects of the COVID-19 pandemic being the major growth inhibitors. Notably, the COVID-19 pandemic had a significant impact on Hexcel's second-quarter sales, operating income and earnings per share. The company has been forced to temporarily suspend its quarterly dividend payouts, share buyback program as well as withdraw its 2020 guidance.

The pandemic's impact has been so immense that Hexcel had to mutually terminate its pending merger deal worth \$6.4 billion with Woodward in April. Notably, synergies from the combination of these two companies might have not brought out the desired results in the current scenario.

- ▼ As of July 2020, global flights are down more than 50% year over year and major airlines are flying well-below their planned capacity levels. International Air Transport Association (IATA) estimates in its latest report that 2020 may witness a 55% annual decline in global airline passenger revenues. This poses a serious threat to growth of aircraft manufacturing stocks along with those that supply parts like Hexcel. The fact that the company is already feeling the heat of the outbreak indicates the risk to the stock. This may have led the company's shares to slump 49.4% compared with the industry's decline of 37.8% in the past year.

Moreover, the company has been lately witnessing greater outsourcing in manufacture of complete wind blades with a rise in cost pressure in the wind industry. This outsourcing is expected to continue. To this end, in the second half of 2020, Hexcel's management expects to witness continued challenges, not only resulting from the pandemic but also from increased cost pressure in the wind energy industry.

737 Max issue and effects of the coronavirus pandemic poses concern for Hexcel Corp.'s growth

Last Earnings Report

Hexcel Q2 Earnings Miss Estimates, Sales Decline Y/Y

Hexcel Corporation reported second-quarter 2020 adjusted earnings of 8 cents per share, which missed the Zacks Consensus Estimate of 20 cents by 60%.

In the quarter under review, the company posted GAAP loss of a penny against the prior-year quarter's earnings of 94 cents.

Significant reduction in demand for its products owing to the effects of the COVID-19 pandemic and the margin mix impact of lower carbon fiber sales resulted in the drop in Hexcel's operating margin. This in turn dragged down the company's quarterly earnings.

Quarter Ending **06/2020**

Report Date	Jul 27, 2020
Sales Surprise	10.23%
EPS Surprise	-60.00%
Quarterly EPS	0.08
Annual EPS (TTM)	2.48

Total Sales

Net sales totaled \$378.7 million, surpassing the Zacks Consensus Estimate of \$344 million by 10.2%. However, the top line witnessed a decline of 37.8% from the year-ago quarter's \$609 million.

The year-over-year deterioration in sales can be primarily attributed to the impacts of the pandemic, which dealt a huge blow to the aerospace industry.

Operational Update

Hexcel's gross margin was 14.5% in the second quarter, reflecting year-over-year contraction of 1320 basis points.

Selling, general and administrative and R&T expenses for the second quarter of 2020 fell 34% year over year, thanks to the company's cost-reduction initiatives, including headcount reductions and lower discretionary spending.

The company's adjusted operating income amounted to \$19.5 million in the quarter compared with \$115.1 million in the year-ago period.

Quarterly Performance

Commercial Aerospace: Net sales were down 51% year over year to \$203.9 million. Lower sales across all major programs, with the Airbus A350 driving the largest quarterly revenue decline resulted in this unit's poor top-line performance.

Space and Defense: Net sales dropped 3% year over year to \$108.4 million on account of lower demand from a number of international space & defense programs.

Industrial: Net sales declined 17.7% year over year to \$66.4 million, primarily due to lower wind energy sales on account of soft demand, arising from the COVID-19 pandemic.

Financial Details

As of Jun 30, 2020, cash and cash equivalents were \$257.2 million compared with \$64.4 million as of Dec 31, 2019.

Long-term debt totaled \$1,265.7million as of Jun 30, 2020, up from \$1,050.6 million as of 2019-end.

At the end of second-quarter 2020, cash generated from operating activities was \$73.6 million compared with \$157.2 million in the prior year.

Post first-quarter 2020, Hexcel had temporarily suspended its share repurchase program and quarterly dividend payouts due to market volatility. So the company made no share repurchase in the second quarter. Its remaining authorization under the share repurchase program as of Jun 30, 2020 was \$217 million.

Hexcel's adjusted free cash outflow at the end of second-quarter 2020 was \$33.2 million compared with \$57.9 million at the end of the prior-year period.

2020 Guidance

Hexcel continues to withhold its financial guidance in the wake of the ongoing market uncertainties as a result of the pandemic.

Valuation

Hexcel Corp.'s shares are down 45.2% in the year to date period and 49.4% over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Aerospace sector are down 41.6% and 29.3% in the year to date period, respectively. Over the past year, the Zacks sub-industry is down 37.8% and the Zacks Aerospace sector witnessed a 28.8% decline.

The S&P 500 index is up 3.3% in the year to date period and 15.7% in the past year.

The stock is currently trading at 25.9X forward 12-month earnings, which compares to 23.4X for the Zacks sub-industry, 21.3X for the Zacks sector and 22.7X for the S&P 500 index.

Over the past five years, the stock has traded as high as 31X and as low as 8.1X, with a 5-year median of 19.1X. Our Neutral recommendation indicates that the stock will perform in line with the market. Our \$43 price target reflects 27.7X forward 12-month earnings.

The table below shows summary valuation data for HXL

Valuation Multiples - HXL					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	25.88	23.36	21.27	22.71
	5-Year High	30.95	23.54	21.27	22.71
	5-Year Low	8.06	12.99	14.17	15.25
	5-Year Median	19.11	17.22	17.24	17.55
P/S F12M	Current	2	0.87	1.16	3.63
	5-Year High	3.13	1.29	1.49	3.63
	5-Year Low	1.01	0.79	0.92	2.53
	5-Year Median	2.31	1.03	1.18	3.04
EV/EBITDA TTM	Current	10	6.95	11.53	12.89
	5-Year High	16.69	12.18	15	12.89
	5-Year Low	6.12	5.99	7.39	8.24
	5-Year Median	12.82	8.77	10.58	10.89

As of 08/05/2020

Industry Analysis Zacks Industry Rank: Bottom 14% (218 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
AAR Corp. (AIR)	Neutral	4
Aerojet Rocketdyne Holdings, Inc. (AJRD)	Neutral	3
CurtissWright Corporation (CW)	Neutral	3
Leidos Holdings, Inc. (LDOS)	Neutral	3
Teledyne Technologies Incorporated (TDY)	Neutral	2
Astronics Corporation (ATRO)	Underperform	4
Heico Corporation (HEI)	Underperform	4
Spirit Aerosystems Holdings, Inc. (SPR)	Underperform	5

Industry Comparison Industry: Aerospace - Defense Equipment				Industry Peers		
	HXL	X Industry	S&P 500	AJRD	ATRO	TDY
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Underperform	Neutral
Zacks Rank (Short Term)	4	-	-	3	4	2
VGM Score	C	-	-	A	A	D
Market Cap	3.35 B	1.19 B	22.93 B	3.41 B	296.48 M	11.91 B
# of Analysts	5	3	14	2	2	2
Dividend Yield	0.00%	0.00%	1.76%	0.00%	0.00%	0.00%
Value Score	B	-	-	A	B	C
Cash/Price	0.08	0.14	0.07	0.32	0.70	0.03
EV/EBITDA	7.67	7.70	13.16	8.87	2.62	20.42
PEG Ratio	3.72	7.34	2.99	NA	NA	NA
Price/Book (P/B)	2.33	1.89	3.20	5.09	1.01	4.13
Price/Cash Flow (P/CF)	7.59	7.42	12.45	15.97	4.77	23.28
P/E (F1)	37.15	28.36	21.78	24.19	NA	33.26
Price/Sales (P/S)	1.63	1.04	2.47	1.71	0.45	3.76
Earnings Yield	2.69%	2.85%	4.33%	4.12%	-33.51%	3.01%
Debt/Equity	0.88	0.39	0.77	0.57	0.59	0.30
Cash Flow (\$/share)	5.29	2.26	6.94	2.72	2.02	13.88
Growth Score	C	-	-	A	A	C
Hist. EPS Growth (3-5 yrs)	8.21%	10.59%	10.46%	35.20%	-23.20%	19.33%
Proj. EPS Growth (F1/F0)	-69.49%	-17.58%	-7.14%	6.21%	-454.40%	-7.61%
Curr. Cash Flow Growth	12.73%	12.73%	5.47%	-8.04%	-23.43%	14.47%
Hist. Cash Flow Growth (3-5 yrs)	9.27%	5.32%	8.55%	70.16%	-8.28%	11.00%
Current Ratio	3.86	2.81	1.32	1.76	2.90	1.97
Debt/Capital	46.81%	33.12%	44.59%	36.13%	37.18%	23.05%
Net Margin	9.48%	4.46%	10.15%	6.46%	-18.79%	12.59%
Return on Equity	14.73%	8.92%	14.46%	19.79%	-0.93%	14.45%
Sales/Assets	0.64	0.73	0.51	0.73	0.86	0.69
Proj. Sales Growth (F1/F0)	-31.45%	-1.25%	-1.68%	4.26%	-36.85%	-2.56%
Momentum Score	F	-	-	C	A	F
Daily Price Chg	5.94%	2.56%	0.59%	0.98%	5.24%	2.43%
1 Week Price Chg	-18.29%	0.00%	0.14%	10.62%	-3.55%	-0.73%
4 Week Price Chg	-9.58%	0.99%	5.31%	18.28%	-0.31%	6.89%
12 Week Price Chg	49.98%	17.68%	19.84%	9.21%	23.27%	1.09%
52 Week Price Chg	-49.49%	-25.45%	2.73%	-13.04%	-65.12%	10.16%
20 Day Average Volume	863,610	172,389	2,098,555	736,473	251,686	240,505
(F1) EPS Est 1 week change	-8.94%	0.00%	0.00%	0.00%	20.51%	0.00%
(F1) EPS Est 4 week change	-14.51%	0.00%	1.10%	5.77%	15.07%	4.25%
(F1) EPS Est 12 week change	-14.51%	-1.96%	1.04%	5.77%	15.07%	4.25%
(Q1) EPS Est Mthly Chg	1,360.00%	0.60%	0.39%	7.69%	44.44%	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	B
Growth Score	C
Momentum Score	F
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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